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Trade Agreements in the Americas: Regionalism Converging to Globalization

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This paper summarizes the evolution of regional trade agreements in the Americas and examines whether they are contributing to globalization or detracting from it. In theory, regional trade agreements may create incentives that deter countries from entering into multilateral negotiations. The paper draws on the political economy literature and takes a "dynamic time-path effect" perspective. The evolution of six regional trade agreements in Latin America are analyzed in detail: LAIA, Mercosur, NAFTA, Andean Community, Caricom, and CACM. This study concludes that regional trade agreements in the Americas have not discouraged the participatory countries' pursuit of multilateral negotiations. Moreover, regional agreements are contributing to a new power balance in the global scene.

Key words: Latin America; multinationalism; preferential trade agreements; regionalism

1. Introduction

In the last thirty years the world trading scene has changed dramatically. Once dominated primarily by a single trade organization, the General Agreement on Tariffs and Trade (GATT), it is now fragmented into a large number of separate trading blocs which co-exist with the GATT and its successor the World Trade Organization (WTO). This fragmentation has become the norm, rather than the exception. According to Paul Krugman, "from 1945 until about 1980, regional trade agreements and the global trade negotiations under the GATT could reasonably be seen as complements rather than substitutes …. Since then, however, the two have moved in opposite directions" (Krugman, 1992 in King ed., 1995, 163).

The pattern of trade agreements in the Americas, particularly in Latin America, fits this trend. From the 1960s to the 1980s several schemes of economic integration of the Latin American region were attempted within the GATT framework. In the post-1980s period, economic integration goes a great deal beyond the scope of the GATT.

Historically, trade agreements in Latin America, both regional and sub-regional, had the objective of contributing to the region's development. This approach to development followed closely the theories put forth by the United Nations' Economic Commission for Latin America and the Caribbean (ECLAC, better known by its Spanish acronym, CEPAL) and the writings of the influential Latin American economist, Raul Prebish. The strategy consisted primarily of pursuing industrialization through "import substitution" and, in the long run, the achievement of economies of scale and the co-ordination of industrial policy through a progressive move towards the formation of a regional market (Macadar, 1992, 72).[1] The Latin American Free Trade Association (Associación Latinoamericana de Libre Comércio, or ALALC), its subsequent organization the Latin American Integration Association (LAIA/ALADI), and the Central American Common Market (CACM) serve as fitting examples.

Although significant progress was achieved in the political and economic relations between the region's countries during the 1960s, 1970s and 1980s, the overall results of the majority of these trade agreements were disappointing. Several events, both political and economic in nature, contributed to the meagre results. For example, military coups experienced by several Latin American countries in the 1960s and the 1970s, the two 1970s oil crises (1973 and 1979), and the debt crisis of the 1980s all had tremendous adverse consequences for the region.

By the mid-1980s, most Latin American countries had abandoned import substitution and had embraced a new development paradigm which includes export promotion, market liberalization, privatization, a shift in regulatory frameworks, democratization, and the aggressive pursuit of foreign direct investments. A new integrationist effort also emerged following in the wake of the signing of the Canada-United States Free Trade Agreement (CUSFTA) in 1988 and the announcement of the Enterprise for the Americas Initiative (EAI) in June 1990. This new era saw the formation of some important new blocs and the revival of old ones. Among the new blocs are the Common Market of the Southern Cone

(Mercosur) and the extension of the CUSFTA to Mexico, forming the North American Free Trade Agreement (NAFTA).

This dynamic environment led to an intense debate among scholars questioning whether this renewed regionalism leads to or detracts from multilateralism. In the economics field this debate starts from the premise that multilateralism—meaning free or freer trade for all—is the desirable outcome, as it maximizes world welfare. In this respect, the economic discourse has evolved from a "static impact effect" analysis—where preferential trade arrangements either divert or create trade—to a "dynamic time-path effect"—where the discussion centres on whether the incentive effects of preferential trade agreements contribute to continued expansion, leading to worldwide free trade, or whether the incentives are in the opposite direction (Bhagwati et al., 1999, xv).

In this paper, the "dynamic time-path effect" framework is used to analyze the new wave of regionalism in Latin America. However, the perspective taken extends the original discourse to include areas other than trade. The proposition is that the recent increase in regional trade agreements in Latin America represents a new era of openness in the region. These arrangements are the first steps towards these countries becoming important players in the world economic system. This thesis is based on four interlinked arguments.

First, these agreements are part of a shift in developmental regime from closed/import substitution to open/global linkage. This shift is reflected in the dramatic increase of foreign direct investments (FDI) into the region (table 1) since 1991.

Table 1 Foreign Direct Investment Inflows into Latin America ($ million US)

Year	Lat. Am.	Lat. Am. minus Mercosur	Lat. Am. minus Mercosur & Mexico	Mercosur	Argentina	Brazil	Mexico
1986	4463	3506	1470	956	574	345	2036
1991	12456	8806	4064	3650	2439	1103	4742
1997	61518	34870	22039	26647	6643	19652	12831
Difference (percent)							
1986-1991	179	151	176	281	324	219	132
1991-1997	394	296	442	630	172	1682	171
Difference between Differences							
	215	145	266	349	-152	1463	39

The dramatic increase in FDI since 1991 suggests that these agreements are not just about trade. Moreover, two recent studies, Hester (1999) and Beaulieu and Hester (1999) show that regional trade agreements in the Americas have an indirect impact on the inflows of FDI. The trade agreements lower country risk, which, in turn, increases the inflows of FDI.

Second, Latin American countries are using membership in regional trade agreements as a strategy to gain more clout in negotiations with the European Union (EU), the United States, and the WTO. The potential for large strategic gains from negotiating as a bloc has been commented on in the Brazilian popular press. For example, recently the weekly magazine *Veja* argued that, by negotiating as a bloc, the four Mercosur countries and the members of the Andean Pact are likely to have a much stronger position vis-à-vis the United States in the upcoming Free Trade Agreement of the Americas (FTAA).

This strategic argument leads to the third argument: it is in the best interests of the Latin American countries to create "open" regional blocs. According to Lustig and Primo Braga,

> For a bloc to be defined as "open," at least two conditions must be met: first, trade and investment barriers to nonmembers must not be raised; and second, new members who are prepared to abide by the same rules as the existing members should be easily accepted (in Weintraub ed., 1994, 24).

The rationale is that, particularly in the case of small countries, the bigger the size of the bloc the more clout the group has. In sum, open regional blocs contribute to the creation of a larger trading group, which, in turn, leads to the globalization process.

Finally, the fourth argument is that the bureaucracy created by the regional trade agreements may help the participating countries function more effectively in the global environment. This is a practical argument. For instance, expertise in sectoral negotiations developed at the regional level is utilized in the same type of undertaking at the multilateral level. Another example is the application of studies conducted by the regional groups' experts to questions that may be relevant in multilateral endeavors.

In this study, these arguments are reviewed and analyzed in the context of a historical examination of six regional agreements in the Americas—ALALC/LAIA, the Andean Community, Mercosur, NAFTA, the Caribbean Common Market (CARICOM), and the Central American Common Market (CACM)—with the objective of finding some answers to the main query of this investigation: Are regional trade agreements in the Americas leading to or detracting from globalization?

The remainder of this paper is organized as follows. Section 2 examines the participation of Latin American countries in the GATT and the reasons behind the search for alternative trading arrangements. Section 3 provides a discussion of the evolution of regional trade agreements in the region, and conclusions are drawn in section 4.

2. Latin America and the GATT

Given the scenario described in the introduction—a proliferation of regional and bilateral agreements in the Americas—one is left wondering what led to this regionalism movement within the context of globalization. In other words, if there was a global organization to which most of the world, including Latin American countries, belonged (see table 2), why create other bureaucracies? The answer to this question lies in the evolution of the GATT.

Table 2 Selected Latin American Countries and GATT Membership

Country	Membership Year
Brazil	1948
Chile	1949
Dominican Republic	1950
Nicaragua	1950
Peru	1951
Uruguay	1953
Jamaica	1963
Guyana	1966
Argentina	1967
Suriname	1978
Colombia	1981
Mexico	1986
Bolivia	1990
Costa Rica	1990
Venezuela	1990
El Salvador	1991
Guatemala	1991
Honduras	WTO – 1995*
Paraguay	WTO – 1995*
Ecuador	WTO – 1996
Bahamas	Not a member
Panama	Not a member

* denotes automatic membership into the WTO on 1 January 1995
Source: gopher://gopher.undp.org:70/00/unearth/organizations/gatt/mcountrie

In the wake of World War II, an attempt was made to negotiate a comprehensive International Trade Organization. The motivation for the creation of such an organization was both philosophical and practical: philosophical, because the framers of the "new world order" believed in trade liberalization, and practical, because the high tariffs which had given rise to the tariff wars of the 1930s were still in place. Unfortunately, the political timing was wrong. The only agreements reached were on a limited subset of trade matters negotiated under the brand new GATT. The larger, more ambitious international trade organization was stillborn. The GATT, by default, became the principal world organization regulating trade (Kerr, 1995, 93).[2]

The GATT's principal objectives were to liberalize international trade in goods and provide a secure environment under which trade could be conducted. After fifty years of existence one could claim that world trade has been liberalized a great deal. However, the pace and scope of these improvements were unsatisfactory in the eyes of many participants, who began to look for alternative arrangements.

There were three principal deficiencies in the GATT process. Negotiations took too long and were too complex, and the dispute settlement mechanism was flawed. Both the liberalization of trade and the ongoing development of rules for trade have been accomplished through successive rounds of negotiations: Annecy Round (1948), Torquay Round (1950-51), Dillon Round (1956, 1960-62), Kennedy Round (1964-67), Tokyo Round (1973-79) and the Uruguay Round (1986-1994) (ibid., 96). As one can observe, these rounds had been getting longer and longer, a reflection of the complexity of issues and divergence of interests of the GATT's 120 member countries. In addition, the GATT was unable to deal with the rapid pace of technological change, the development of the service sector, and the increase in direct and indirect international investment.

These and a multitude of other problems led to negotiations and an agreement in 1993 to form a World Trade Organization. The WTO has been operational since 1995. Membership in the WTO was extended to all GATT members. The WTO has addressed several of the problems mentioned previously. It is a permanent organization with a much better conflict resolution procedure than its predecessor. Added to the GATT (which is still responsible for trade in goods) were the GATS (General Agreement on Trade in Services) and the TRIPS (Agreement on Trade-Related Aspects of Intellectual Property). Although since its creation the WTO has been the forum for successful negotiations to open markets in telecommunications and in information technology equipment, the complete success of its dispute settlement mechanism is questionable. According to the information provided on the organization's website:

> Of the 150 cases, about 30 have been withdrawn following consultations between countries in dispute; over 100 are going through the procedure of con-

> sultation, panel adjudication or appeal; about 20 are in the final stage of implementing a solution; four have been settled and the solution implemented; seven have been closed without any need for action to be taken (FAQs, 1999, 2 of 5).

Note that of the 150 cases, 30 have been withdrawn, which leaves 120. Subtracting the 100 cases that are still going through the process, only 20 remain. At this point the math gets complicated, as the WTO claims 20 are in final implementation stages, while there are still 11 which have been settled or closed. Nonetheless, it has to be recognized that solving disputes and negotiating with 139 countries is a complicated and lengthy proposition.[3] Moreover, the trade world is far different than it was at the beginning of the Uruguay Round in 1986. Countries that belong to some of the regional trade arrangements negotiate at the WTO as a group; consequently, the bargaining process has been irrevocably changed.[4]

Although the difficulties with the negotiations of the GATT/WTO discussed above in part explain the proliferation of trade agreements, they do not explain the different types of regional arrangements formed in the Americas. To understand the different types of arrangements that have formed, one must look at the provisions of the GATT's Article XXIV. This clause permits the formation of preferential trading arrangements, such as free trade areas (FTAs) and customs unions (CUs), provided they meet certain conditions. Note that FTAs and CUs violate the GATT's key principle of Most Favoured Nation treatment. The basic notion is that discrimination is permitted in exchange for full liberalization. Consequently, these trading arrangements must cover "substantially all trade" (Lawrence in Schott ed., 1996, 44). This was a very contentious issue for developing countries, as it required that any type of arrangement be either a "full-fledged" free trade area or a customs union. Consequently, developing countries were forced into far too ambitious integration schemes. It took them almost 20 years (Tokyo Round, 1973-79) to reach a compromise with the developed world. As section 3 shows, Article XXIV shaped the original regional arrangements in Latin America.

Clearly, regional trade agreements have led to a change in the world trading scene. This time however, although the alliances are clearly regional in nature, the motivations for the recent agreements are very different from those of the 1960s and 1970s. In Latin America, every country is busy forging alliances with its neighbours: Mexico looking north, Brazil looking south, and Bolivia looking all around.

Mexico's new partnership in NAFTA has given it access to one of the most coveted markets in the world. Perhaps Mexico's strategy is to use this access to become the link between the rest of Latin America and North America. Brazil, on the other hand, has chosen to pursue a connection with North America from a strictly South American position, through the Mercosur. Chile's tactics are to gain access to as many regions as possible.

Among its most important alliances are its associate membership in the Mercosur and the Free Trade Agreement with Canada, both achieved in 1996.

Certainly, trade agreements are being used as a means to gain access to markets. But is this all they are doing? Are regional trade agreements in the Americas being forged as a strategy for positioning in the world? A first step in answering this question is to gain an understanding of the regional trade agreements in the region.

3. The Evolution of the Regional Trade Agreements in the Americas

Between 1960 and the late 1970s there were several attempts at economic integration in Latin America. Most notably, the Latin American Free Trade Association (Asociación Latinoamericana de Libre Comércio, or ALALC) was signed originally by Argentina, Brazil, Chile, Mexico, Paraguay, Peru, and Uruguay, and the Central American Common Market (CACM) was signed in December of 1960 between Guatemala, Honduras, El Salvador, and Nicaragua.[5] This integration wave also touched the Caribbean, where in 1965 Antigua, Barbados and Guyana formed the Caribbean Free Trade Association (CARIFTA), which was augmented by eight other countries in 1968 and renamed the Caribbean Common Market (CARICOM) in 1973. Some countries that belonged to the ALALC decided to form a common market in order to speed up the integration process. This effort resulted in the formation of the Andean Pact (Pacto Andino) in 1969. The original signatory countries were Chile, Colombia, Ecuador, and Peru.[6] Unfortunately, for reasons explained previously, the results of these agreements were very disappointing.

Currently, the majority of the countries in the Latin American and Caribbean region belong to one of four regional integration arrangements whose stated objective is to develop a common market. The CACM, CARICOM and the Pacto Andino have been revived, and Brazil, Argentina, Uruguay and Paraguay have formed the Mercosur. As mentioned, Mexico and Chile have taken a different path. Mexico has decided to formalize its economic integration with its northern neighbours, the United States and Canada, by signing the North American Free Trade Agreement (NAFTA). Although Chile is probably a likely candidate to join NAFTA, difficulties in negotiations with the United States have prevented the process from occurring in an expeditious fashion.[7] Chile has signed bilateral free trade agreements with Colombia, Mexico, Venezuela, and Canada, as well as a preferential trade agreement with the Mercosur. Table 3 presents an outline of these various regional trading arrangements in the Americas.

Table 3 Regional Agreements in the Americas

Multilateral	Regional Integration	Regional Customs Unions	Regional Free Trade Areas
WTO/GATT	LAIA/ALADI	ANDEAN COMMUNITY	NAFTA
		MERCOSUR	
		CARICOM	
		CACM	

Apart from the regional agreements outlined above, many bilateral agreements have also been signed. In fact, so many trading arrangements have been formed or revitalized since 1990 that one is left with the impression that several of them must be redundant, such as the FTA signed by El Salvador, Guatemala, and Honduras; or contradictory, such as the bilateral FTAs signed by Colombia and Venezuela with Chile. Yet in practice, although the duplication and complication of bureaucracy is far from ideal, these agreements serve a useful purpose. They often are used as an instrument of pressure to goad a slow-moving member of the original agreement to speed up the pace of change (Lustig, Nora and C.A. Primo Braga in Weintraub ed., 1994, 25).

Moreover, Latin American countries, like the rest of the world, are signing Bilateral Foreign Investment Protection Agreements (FIPAs) at warp speed.[8] According to the United Nations Conference on Trade and Development (UNCTAD), of the 1500-plus FIPAs in existence at the end of 1997, more than three-quarters date from the 1990s (UNCTAD, 1998, 117). The figures for Latin America are even more staggering: three FIPAs were signed in the 1980s and fifty-three in the 1990s (up to the end of 1998). Also, most of the regional trade agreements in the Americas have clauses similar to the one found in FIPAs.

The proliferation of trading and investment arrangements can also be interpreted as a “race” to be included in blocs. In the early 1990s some economists believed that Latin American countries were only using the sub-regional agreements as a stepping stone towards ascension into NAFTA, as they perceived the United States to be more willing to negotiate with a group rather than with individual countries (Lustig, Nora and C.A. Primo Braga in Weintraub ed., 1994, 24). Other authors however, believed that this desire to become a member of NAFTA was only a reflection of “small, though influential, groups now in government in different countries” (Naim, Moises in Weintraub ed., 1994, 48). The debate now, a number of years later, has evolved considerably.

Joining NAFTA is seen as a lost cause even by the most willing countries, as in the case of Chile. This is probably a consequence of the lack of fast-track authority of the Clinton administration, combined with the realization by most Latin American countries that the changes necessary to meet the conditions required for NAFTA membership might not be compatible with their own objectives.[9] As it was, the successful signing of NAFTA was due to a particular set of circumstances. Mexico and Canada already had a high level of economic integration with the United States, Mexico has a large constituency in the United States that the Mexican government was capable of mobilizing, and finally, the Mexican government, because of the unique executive grip it has over the legislature, the unions, the communications and the private sector, was able to overcome domestic opposition. It is unlikely that other Latin American governments can deliver the same type of concessions without facing a great deal of opposition at home. The solution to the issues mentioned above was found by reviving the Enterprise for the Americas initiative, now the Free Trade Agreement of the Americas (FTAA). These negotiations, which are expected to be completed in 2005, involve all of the countries in the Americas, with the exception of Cuba. In addition, the Mercosur has become considerably more powerful in the last five years. Among several initiatives, it is presently negotiating an agreement with the EU in conjunction with its active participation in the FTAA proceedings.

Each of the Latin American trade agreements mentioned above is discussed in more detail in the technical annex. Note that the observed increasing regionalism within globalization highlights the importance of the classification of "open" or "closed" blocs, alluded to earlier. In principle, none of the regional trading arrangements is raising barriers to non-members. Therefore, they fulfill the first condition for definition as open blocs. As far as the second condition is concerned—new members who are prepared to abide by the same rules as the existing members should be easily accepted into the bloc—some of these arrangements, particularly NAFTA, appear to be closed. Although Mercosur is definitely more open than NAFTA, it is not completely open either. Bolivia and Chile were accepted as associate partners in 1996; however, the accession process is full of twists and turns—possibly the equivalent to non-tariff barriers to trade. This fact adds to the uncertainty of the future direction of the region. Nonetheless, it seems that the region is moving slowly towards enlarging the "regional market."

4. Conclusion

This paper has sketched a Latin American trade arrangements map that would confuse even people familiar with trade in the region. However, clearly these arrangements are about a lot more than just trade. Embedded into each regional agreement are the aspirations for development and global positioning of each member country.

The multiple layering in the present scenario shows that Latin American countries have embraced trade liberalization and openness with the same gusto as they once embraced policies of import substitution. Although the implementation of this new position has not occurred evenly across countries, all are using trade agreements to entrench these changes. Although one should always be cautious in making definitive statements, especially with regard to Latin America, it appears that this liberalization process is irreversible.

This process is also changing the "market" landscape of the region. The talk is not only of Argentina and Brazil, but of Mercosur; not just of Mexico, but of NAFTA. It appears that this is fertile terrain for the growth of additional linkages beyond the traditional trade – comparative advantage paradigm.

Moreover, Latin American countries are becoming important players in the world economy. The proposition that the new regional trade agreements in Latin America represent a new era of openness in the region has been amply supported by this study. Consequently, this new regionalism can be interpreted as a move towards multilateralism. What has changed is that this time around, countries are using their regional position strategically. Now, this is their strength not their weakness.

Regional trade agreements in the Americas are influencing areas far beyond their original intent, in ways that have not been anticipated. In the end it is all about development. Ironically, the new development paradigm, which is exactly opposite to the one originally suggested by Raul Prebish, might ultimately achieve his dream: a Latin American integrated market in a global village.

Endnotes

1. Import substitution: in order to promote domestic industrialization and conserve scarce foreign exchange, tariffs and quotas are used to limit or at times remove competing imports. The aim is to establish manufacturing industries that initially can be expanded to supply the domestic market, and later to develop an export trade. (Adapted from *The Harper Collins Economics Dictionary,* 1991, 240.)
2. It is important to note that up until the end of the Uruguay Round a number of countries, primarily Eastern European countries, had not joined the GATT.
3. 139 countries are currently members of the WTO and 29 others have requested to join the organization. Their applications are currently being considered by accession working parties.
4. Any countries belonging to an arrangement constituted as a customs union or common market (definitions for all types of trade arrangements are provided in the technical annex) negotiate at the WTO as a group.
5. In 1961 Colombia and Ecuador joined ALALC, while Venezuela and Bolivia did so in 1966 and 1967, respectively.
6. In 1973 Venezuela became a member and in 1976 Chile withdrew.

7. The Brazilian newspaper *Jornal do Brasil* of 8 August 1999 announced that Chile had "given up" pursuing negotiations to enter NAFTA. Instead, the article claimed, Chile was beginning free trade agreement negotiations directly with the United States (http://www.jb.com.br).
8. FIPAs are also known as Bilateral Investment Treaties (BITs).
9. Fast-track legislation gives the U.S. Congress the authority to have an "up or down" vote on a trade agreement negotiated by the administration. That is, with fast-track, Congress votes "Yay" or "Nay" on a trade agreement negotiated by the U.S. Administration and cannot alter portions of an agreement. Without fast-track, Congress has the right to approve parts of the agreement while rejecting others. Thus, lacking fast-track authority, the U.S. Administration cannot negotiate a trade agreement in good faith.

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The technical annex to this paper, pages 123-136, is available as a separate document.